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COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

AT RICHMOND, MARCH 30, 2001

COMMONWEALTH OF VIRGINIA, ex. rel.

STATE CORPORATION COMMISSION

CASE NO. PUE000740

Ex Parte: In the matter
concerning a draft plan
for phase-in of retail
electric competition

ORDER CONCERNING PHASE-IN OF RETAIL CHOICE

On December 21, 2000, the Commission issued an Order ("the December 21 Order") in this matter prescribing notice and inviting comments concerning the Commission Staff's report and draft plan ("the draft plan") for the transition to full retail choice for electric generation. The Commission's development and adoption of such a plan is expressly required by the Virginia Electric Utility Restructuring Act.¹ The December 21 Order invited comment on the draft plan by interested parties, such comments to be filed with the Clerk of this Commission on or before February 15, 2001. The Order also provided interested parties an opportunity to request a hearing or oral argument on the draft plan.

The following parties filed comments on or before February 15, 2001: the Virginia Committee for Fair Utility Rates and the Old Dominion Committee for Fair Utility Rates ("the Committees"), filing jointly; the New Power Company; Washington Gas Energy Services, Inc.; Kentucky Utilities Company d/b/a/ Old Dominion Power Company ("Kentucky Utilities"); Virginia Electric and Power Company ("Virginia Power"); Potomac Edison Company d/b/a Allegheny Power ("Allegheny"); Appalachian Power Company d/b/a American Electric Power Company ("AEP Virginia"); Ladd Furniture, Inc.;

¹ § 56-577 A 2 a.

Henkel-Harris Co.; Webb Furniture Enterprises, Inc.; Delmarva Power and Light Company ("Delmarva"); Office of the Attorney General, Division of Consumer Counsel; the Virginia, Maryland & Delaware Association of Electric Cooperatives, and its Virginia member cooperatives ("the Cooperatives"); Northern Virginia Electric Cooperative; and AES New Energy, Inc. Virginia Power requested oral argument on the issues presented by the draft plan, while the Cooperatives requested an evidentiary hearing.

On February 26, 2001, the Staff of the Commission filed a Supplemental Staff Report on the Schedule for Transition to Retail Access ("draft plan supplement"), making three modifications to such plan. According to the Staff, the modifications responded to information and recommendations contained in comments filed by interested parties in response to the draft plan.

Thereupon, the Commission, by Order dated February 26, 2001, requested further responses from interested parties concerning the draft plan supplement. This order established a March 5, 2001, filing deadline for such responses. Pursuant to that Order, further responses were timely filed by the Committees, Virginia Power and the Cooperatives. While the Cooperatives' initial comments requested an evidentiary hearing, their further response indicated that they no longer required an evidentiary hearing in this matter so long as the Commission adopted the Staff's recommendations in the draft plan supplement.²

Accordingly, by Order dated March 7, 2001, the Commission scheduled an oral argument in this matter for March 20, 2001. The following parties appeared and were represented by counsel at that argument: Virginia Power; AEP Virginia; the Office of the Attorney General's Division of Consumer Counsel; the Committees; the Cooperatives; Allegheny; the New Power Company; and Delmarva.

² The Commission Staff has modified its earlier recommendation that the Cooperatives complete their phase-in of retail choice for electric generation services by January 1, 2003. The draft plan supplement filed by the Staff now recommends that the Cooperatives be given until January 1, 2004, to complete the phase-in within their respective service territories. However, the Cooperatives' withdrawal of their request for an evidentiary hearing was made contingent upon the Commission's inclination to follow the Staff's recommendations concerning the Cooperatives' phase-in schedule. The Commission ruled in its March 7, 2001, Order that it would hold that request in abeyance pending oral argument.

Briefly summarized, the Staff's draft plan as modified by the draft plan supplement provides first that the service territories of Delmarva, AEP Virginia, and Allegheny will be fully opened to choice for retail generation services on and after January 1, 2002. The Staff has characterized this as a "flash cut" to retail choice inasmuch as there would be no transition or other phase-in. Thus, under this flash-cut proposal—affirmatively proposed by the affected utilities—all of the retail electric customers in these utilities' service territories would be permitted to choose between their incumbent electric utilities and any competitive service providers ("CSPs") on and after January 1, 2002. The extent of competitive choice, of course, would be contingent upon the availability of competitive service offerings by CSPs operating in those service territories.

With respect to the Cooperatives, the Staff has recommended that these utilities be permitted to phase in retail choice in their service territories during the two-year period, January 1, 2002, through January 1, 2004. This recommendation corresponds to the phase-in period requested by the Cooperatives in their filing in this matter. While the Staff had initially proposed that their phase-in be completed by January 1, 2003, the Staff now recommends a full two years on the bases that (i) most of the Cooperatives will require additional time to upgrade information and communications systems, e.g., electronic data interchange, or EDI systems, and (ii) the experience in other states—particularly in Pennsylvania—suggests that cooperatives will not drive the development of competitive markets, and thus the speed with which their service territories are opened may not be a significant factor in the development of such markets.

The Staff has also recommended that Kentucky Utilities be permitted to phase in retail choice within its service territories during the period January 1, 2002, through January 1, 2004. Responding to this company's filing in this matter, the Staff agrees that the small size of Kentucky Utilities' service territory, coupled with the fact that this utility is interconnected with no other Virginia utility, and further combined with the low level of restructuring activity currently occurring in Kentucky (where most of this company's operations are located), suggests that competition in the service territory of this incumbent will play—at best—a modest role in the development of a competitive retail generation market in

Virginia. Consequently, the Staff has proposed that Kentucky Utilities be provided two years to open its service territory to competition.

With respect to Virginia Power, the Commonwealth's largest incumbent electric utility, the Staff has proposed that this company begin a one-year phase-in on January 1, 2002, completing the same by January 1, 2003. Virginia Power voiced opposition to the Staff's recommended one-year phase-in for this company, proposing instead that it be given a full two-year period in which to implement a three-part, regional phase-in of competitive choice for its residential customers in combination with a three-part, state-wide phase-in of larger commercial and industrial customers (GS3 and GS4). We note, however, that disagreement over Virginia Power's phase-in interval reached beyond the company and the Commission's Staff. The Committees, for example, proposed a flash cut for the phase-in of retail choice in Virginia Power's service territory commencing January 1, 2002. Except with respect to the phase-in period, the Staff and Virginia Power are in agreement concerning virtually every aspect of Virginia Power's proposed phase-in plan.

Additionally, while not part of Virginia Power's phase-in plan as initially proposed, the company has indicated its willingness to include smaller commercial (GS1 and GS2) plus worship site customers in the three-part, state-wide phase-in of commercial and industrial customers. The Staff supports this proposal.

At the oral argument in this matter, the issue of Virginia Power's phase-in dominated the debate. The company based its opposition to the Staff's recommendation of a one-year phase-in on a procedural basis and on substantive grounds. On the procedural level, the company asserted that the Staff had failed to satisfy § 56-577 B 1, arguing that the one-year phase-in constitutes an "acceleration" and that the Staff had made no showing in its phase-in plan that this "acceleration" was justified on the basis of reliability, safety, communications or market power.³ Virginia Power further asserts that it needs a full two-year period to phase-in retail choice throughout its entire service territory.

³ § 56-577 B 1 provides, in pertinent part, that "[T]he Commission may delay or accelerate the implementation of any of the provisions of this section, subject to the following: 1. Any such delay shall be based upon considerations of reliability, safety, communications or market power."

Two ancillary issues before the Commission related to the Virginia Power phase-in plan concerned (i) the establishment of a "waiting list" for large commercial and industrial customers (GS3 and GS4) who miss inclusion in a particular phase because of the MWh-based quotas imposed for each phase, and (ii) the willingness of Virginia Power to include GS1, GS2, GS3, GS4 plus worship site customers in the three-part, state-wide phase-in initially proposed for GS3 and GS4 customers, only.

NOW THE COMMISSION, upon consideration of the Staff's draft plan, and the draft plan supplement, the comments and responses of parties concerning such draft plan and draft plan supplement, and upon consideration of the oral argument offered by the parties on March 20, 2001, is of the opinion that the Staff's proposed revised phase-in schedules for Virginia's incumbent electric utilities as outlined above, should be adopted for the reasons set forth in the Staff's draft and draft plan supplement. Additionally, the Commission is of the opinion that GS1, GS2, GS3, GS4 and worship site customers in Virginia Power's service territory should be phased in as part of that company's state-wide phase-in initially proposed for GS3 and GS4 customers only. However, we will not require a waiting list for GS3 and GS4 customers in the Virginia Power phase-in as has been recommended by the Staff.

Inasmuch as the phase-in schedules we approve today for Delmarva, Allegheny, AEP Virginia, the Cooperatives, and Kentucky Utilities conform to the Staff recommendations as well as the express desires of the companies themselves, we will provide no further comment thereon in this Order except to state that we adopt the Staff's rationale therefor in these cases.

With respect to Virginia Power, we will not adopt the Committees' recommendation that this utility flash cut to retail choice on January 1, 2002, nor will we adopt the company's proposal to phase in competition over the two-year period, January 1, 2002, to January 1, 2004. Instead, we will adopt the Staff's proposal: a one-year phase-in to be completed by January 1, 2003.

Virginia Power is Virginia's largest incumbent electric utility with over 1.75 million residential electric customers. Making the Commonwealth's largest electric market competitive as soon as possible is obviously a critical link in the success or failure of the development of a competitive market for retail generation in Virginia as a whole. Retail choice pilot programs in the northern and central

regions of this company's service territories underscore the emphasis this Commission has placed on moving this company and its customers toward a competitive retail market as quickly as practicable.

We find that completing Virginia Power's phase-in over a one-year period is a critical goal that can and should be realized. While the company raised objections to a one-year phase-in on the basis that it needs the extra time to get ready, nowhere in its filings in this matter nor in oral argument offered on the company's behalf did the company identify any specific or substantial impediments thereto.⁴

By January 1, 2002, the company will have had all the benefits of one and one-half years of operational pilot programs in which to develop, test and implement necessary systems to support retail customer choice within its service territory when full choice begins in January 1, 2002.⁵ Significantly, the company did not assert that it could not complete the phase-in by January 1, 2003, as recommended by the Staff. Moreover, the company's counsel stated at the oral argument that the company would be ready to implement Phase I of its phase-in plan on January 1, 2002—the largest component of its phase-in, involving over 600,000 residential customers and 6 million MWh of commercial and industrial load. (transcript pg. 19). Consequently, the combined experience of pilot programs together with necessary preparation of systems and processes for the company's first phase lead us to conclude that the company can achieve full phase-in by January 1, 2003.

⁴ The company did point out in its filings and at oral argument, difficulties an affiliate (Dominion East Ohio Gas) had experienced in the phase-in of an Ohio natural gas pilot program (trans. pp. 16, 17). However, from all accounts the affiliate's call center difficulties appear related to a unique set of circumstances unlikely to be duplicated (a competitive supplier's attractive offer for both natural gas and electricity made available for a very short period), and we were further advised at the oral argument by Staff counsel that Ohio's flash cut phase-in of retail choice for electricity (commenced on January 1, 2001) was going smoothly according to Ohio Public Utility Commission representatives. See, transcript at 59, 60. The company's counsel also stated at the oral argument that some of the necessary processes and systems to accommodate full choice in the Virginia Power service territory do not yet exist. However, the company's counsel also said that the company could and would be ready to implement the first and largest phase of its phase-in plan on January 1, 2002. Evidently, substantial progress in the development and implementation of critical systems and processes will underpin the January 1, 2002, phase-in roll-out.

⁵ We are concerned that during oral argument, the company's counsel indicated that the company was still manually billing some of the large commercial and industrial customers who have chosen competitive suppliers in its retail choice pilot programs rather than automating its billing systems. (Transcript, pg. 73) We would encourage the company to make use of this time in its pilot programs to introduce system automation in this respect, and wherever else possible. The company's first phase commencing January 1, 2002, involves 600,000 residential customers and 6 million MWh of commercial and industrial load. Critical systems such as automated billing must be in place by that time, in any event; we will look forward to the company's future reports describing their progress in this and other key areas.

With respect to Virginia Power's procedural argument that the Staff's recommendations fail to satisfy the provisions of Virginia Code § 56-577 B 1, we find that this argument is without merit. First, in our view, the company failed to make a credible argument that the Staff's proposed one-year phase-in for full retail choice within the Virginia Power service territory is an "acceleration" under the statute. As the Committees, the Attorney General and the Staff pointed out in their filings and during the oral argument, the language in § 56-577 A 2 a requires that Virginia's incumbent electric utilities phase-in of retail choice be completed "by January 1, 2004." Thus, any date prior to January 1, 2004—such as the January 1, 2003, date proposed by Staff—would satisfy that criteria. In effect, to be an acceleration, a phase-in would have to employ a start date before January 1, 2002. A delay would constitute a phase-in completion date beyond January 1, 2004.

However, putting aside the procedural objection, we note—as also pointed out by the Committees in their filings and emphasized by counsel for the Staff at the hearing—that the record developed in this matter (comprising the Staff's report and supplemental report, the parties' filings in response thereto, and the argument of counsel for the parties at the hearing) supports the Staff's recommendations. In our review of this record, we took into consideration the following:

(i) communications, education, and marketing, (ii) safety and reliability, (iii) market power, and (iv) the practical ability of the incumbent utility to phase in retail choice. Not surprisingly, there is overlap between the criteria we apply here in establishing the phase-in schedule, and those factors § 56-577 B 1 would require us to consider in the case of acceleration or delay.

With respect to communication, education, and marketing, for example, both Allegheny and The New Power Company (a CSP) stated in their filings and at the oral argument in this matter that a flash cut to competition is beneficial to the development of competition in a service territory because it simplifies consumer education for electric consumers, and it assists CSPs in the development and execution of their marketing plans to attract customers. Indeed, the Staff noted in its report that one of the distinct advantages of an expedited transition is the simplification of consumer education. This is a consideration we believe justifies a phase-in of one year for Virginia Power.

Similarly, the Staff report indicates that the immediate introduction of choice on a date certain helps to attract competitive suppliers. Ultimately, the attraction of competitors—as emphasized in the Committees' comments—will help mitigate incumbent electric utilities' residual market power, thereby encouraging the development of a competitive market. Consequently, we conclude that a short phase-in period for the state's largest electricity market is critical to encourage new market entrants and the development of a truly competitive market.

Moreover, with respect to "reliability" and "safety," we see nothing in the record developed on these issues, to date, that augurs against the use of a one-year phase-in for Virginia Power. In any event, however, with respect to these and the other considerations outlined above, Virginia Power and the other incumbent electric utilities will have ample opportunity to alert us to any specific phase-in problems through the reporting processes we establish in this Order. Moreover, in the event that the company desires to extend the phase-in beyond January 1, 2003, it may request such an extension. If, however, the company desires to delay the completion of its phase-in beyond January 1, 2004, it may make an application under § 56-577 B 1 requesting authorization to do so, taking into account the criteria outlined therein (safety, reliability, communications or market power). In the meantime, however, we believe that the company's implementation of its pilot programs demonstrates its practical ability to implement full retail choice throughout its service territory by January 1, 2003.

Finally, with respect to the Virginia Power phase-in, we note that at the hearing, Virginia Power's counsel offered, for the first time in this proceeding, an offer of compromise between the one-year phase-in proposed by the Staff, and the two-year period advocated by Virginia Power. In summary, the compromise would provide that (i) the first phase of Virginia Power's phase-in (identical in both Staff and company proposal) would be implemented in January 1, 2002, and (ii) at or about April 2002 the Commission would convene a hearing in this docket to determine, at that juncture, whether the phase-in to competition in Virginia Power's service territory should be completed within the remainder of the year or whether a full two-year period should be required.

While we appreciate the company's efforts to find common ground with the Staff, it would appear that Staff views the one-year phase-in as a compromise proposal to begin with and it was so

characterized by its counsel at the oral argument. However that may be, the uncertainty that would be introduced by the company's compromise proposal would not, in our view, be helpful to CSPs in developing their marketing strategies for this important service territory, nor would it be helpful to Virginia Power's consumers who would be left uncertain, if not confused, as to the timing of customer choice. Consequently, the question mark such a proposal's adoption would leave over the entire phase-in of this company's service territory militates against its endorsement by this Commission.

To assist the Commission in carrying out its oversight of the phase-in of retail choice, we will require all incumbent electric utilities subject to this Order to provide periodic reports concerning the phase-in of retail choice in their service territories. This, in our view, is the best way for the Commission and these utilities to ensure that all necessary processes and systems for implementing retail choice are identified, developed (where needed), introduced, and further refined, as necessary.

Accordingly, each such utility shall furnish quarterly updates concerning the status and progress of phase-in implementation within its service territory, with the first of such reports due on or before May 15, 2001. Such reports shall be furnished to the Commission and the Commission's Staff not later than the fifteenth of every month following the end of each calendar quarter thereafter (e.g., July 15, October 15, January 15, April 15, etc.), through and including the twelve-month period following the completion of each utility's full phase-in of retail choice throughout its service territory. However, those utilities commencing the phase-in of retail choice on January 1, 2002, shall furnish their reports concerning 2001's fourth quarter, on or before December 15, 2001.

Each such phase-in status report shall: (i) identify and describe critical systems and processes each utility needs for phase-in of retail choice within its service territory, which listing shall be updated and supplemented in each report, and (ii) provide a status report concerning each such system or process, identifying (a) items completed, and (b) items not completed, providing estimated completion dates and a brief description of activities underway to ensure their completion. Following each utility's commencement of phase-in, such reports shall also summarize the utility's experience with the phase-in of retail choice, describing any and all significant problems encountered together with actions taken, and

to be taken, by the utility to resolve them and when it is anticipated that such problems will be resolved. Changes in systems and procedures shall also be described

In addition to the reporting requirements set forth above, the Cooperatives and Kentucky Utilities shall also summarize in each quarterly report due under this Order, and in detail, their timelines for phasing in retail choice within their respective service territories on or before January 1, 2004.

Accordingly, IT IS ORDERED THAT:

(1) The Staff's Revised Recommended Plan for the Transition to Retail Access, appended as Attachment B to the Staff's Supplemental Staff Report on the Schedule for the Transition to Retail Access dated February 26, 2001 is adopted, except as otherwise provided in this Order;

(2) The Virginia Power state-wide phase-in for GS3 and GS4 customers shall also include GS1, GS2, and worship site customers.

(3) Delmarva, AEP Virginia, Allegheny, Virginia Power, the Cooperatives, and Kentucky Utilities shall provide periodic reports concerning preparation for and implementation of phase-ins within their service territories as provided in this Order.

(4) This matter is continued for further orders of the Commission.